

**Alabama Drinking Water
Finance Authority**

Component Unit Financial Statements

For The Year Ended September 30, 2010

Alabama Drinking Water Finance Authority
Table of Contents
September 30, 2010

	<u>Page</u>
INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENTS	1
MANAGEMENT'S DISCUSSION AND ANALYSIS	2 - 3
BASIC FINANCIAL STATEMENTS	
AUTHORITY-WIDE FINANCIAL STATEMENTS	
Statement of Net Assets	4
Statement of Activities	5
FUND FINANCIAL STATEMENTS	
Statement of Net Assets - Proprietary Fund	6
Statement of Revenues, Expenses, and Changes in Fund Net Assets - Proprietary Fund	7
Statement of Cash Flows - Proprietary Fund	8 - 9
Notes to Financial Statements	10 - 21
SUPPLEMENTARY INFORMATION	
Schedule of Expenditures of Federal Awards	22
Notes to Schedule of Expenditures of Federal Awards	23
COMPLIANCE SECTION	
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <u>Government Auditing</u> <u>Standards</u> .	24 - 25
Independent Auditors' Report on Compliance with Requirements that Could Have a Direct and Material Effect on Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133.	26 - 27
Schedule of Findings and Questioned Costs	28



Carr, Riggs & Ingram, LLC
1117 Boll Weevil Circle
Enterprise, Alabama 36330

Mailing Address:
P.O. Box 311070
Enterprise, Alabama 36331

INDEPENDENT AUDITORS' REPORT ON FINANCIAL STATEMENTS

Board of Directors
Alabama Drinking Water Finance Authority
Montgomery, Alabama

(334) 347-0088
(334) 347-7650 (fax)
www.cricpa.com

We have audited the accompanying financial statements of the business-type activities, the major fund, and the remaining fund information of the Alabama Drinking Water Finance Authority (the "Authority"), a component unit of the State of Alabama, as of and for the year ended September 30, 2010, which collectively comprise the Authority's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in **Governmental Auditing Standards**, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing accounting principles used and significant estimates made by management, as well as evaluating the overall basic financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities, the major fund, and the remaining fund information of the Authority as of September 30, 2010, and the respective changes in financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with **Governmental Auditing Standards**, we have also issued our report dated February 8, 2011, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with **Governmental Auditing Standards** and should be considered in assessing the results of our audit.

Our audit was performed for the purpose of forming an opinion on the financial statements that collectively comprise the Authority. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U. S. Office of Management and Budget (OMB) Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations" and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Carr, Riggs & Ingram, L.L.C.

CARR, RIGGS & INGRAM, L.L.C.

Certified Public Accountants

February 8, 2011

MANAGEMENT'S DISCUSSION AND ANALYSIS

The Alabama Drinking Water Finance Authority (the Authority) was established in 1997 to provide a self-perpetuating source of low interest loans for the construction of public water treatment and distribution facilities needed to meet the public health goals of the Safe Drinking Water Act. The Authority is operated by The Alabama Department of Environmental Management serving as agent for the Authority. The following discussion provides an overview of the financial position and results of operation for the Authority as of September 30, 2010. For more detailed information, please refer to the financial statements including the Notes to the Financial Statements.

Overview of the Financial Statements

The Authority operates as a Proprietary Fund and presents the following basic financial statements: Statement of Net Assets, Statement of Activity, Statement of Net Assets - Proprietary Fund, Statement of Revenues, Expenses, and Changes in Net Assets - Proprietary Fund and Statement of Cash Flows –Proprietary Fund. The statements are prepared using the accrual basis of accounting. Revenues are recognized when earned and expenses are recognized when incurred, regardless of when cash is received or expended. Investments are reported at fair market value.

The Proprietary Fund statements provide financial information about the Alabama Drinking Water Finance Authority which the Alabama Department of Environmental Management operates like a business.

Statement of Net Assets - Proprietary Fund – Includes all assets and liabilities of the Authority and provides a snapshot of the financial position of the Authority at the end of the fiscal year. Assets less liabilities results in net assets that are restricted and used in assuring the perpetuation of the Authority. Net assets are comprised primarily of loans receivable that are not obligated to a bond issue, and cash or short term investments pledged to loans that are in the process of closing.

Statement of Changes in Net Assets – Proprietary Fund – Reports all additions and deductions of the Authority for the fiscal year. Additions are primarily comprised of loan and investment income and federal awards. Deductions are mainly bond interest expense. Additions minus deductions provide the change in restricted net assets for the fiscal year. The change in restricted net assets plus the beginning restricted net assets results in the restricted net assets available for the perpetuation of the Authority.

The Notes to the Financial Statements include organizational description, a summary of significant accounting policies, information on cash and investments, loans receivable, payables to municipalities, long term debt, arbitrage, related parties and prior period corrections.

COMPARATIVE SUMMARY STATEMENTS

Statement of Proprietary Net Assets

<i>September 30,</i>	2010	2009	Variance	% increase (decrease)
Assets				
Cash and cash equivalents	\$ 45,644,583	\$ 40,477,264	\$ 5,167,319	13%
Receivables	241,198,699	241,825,798	(627,099)	0%
Investments	54,763,753	55,123,535	(359,782)	(1%)
Unamortized items	9,320,933	6,846,632	2,474,301	36%
Capital assets	-	14,602	(14,602)	(100%)
Total assets	350,927,968	344,287,831	6,640,137	2%

Liabilities				
Accrued liabilities	2,222,776	2,400,996	(178,220)	(7%)
Payable to municipalities	26,376,453	26,352,925	23,528	0%
Bonds payable, net	173,550,016	179,878,954	(6,328,938)	(4%)
Total liabilities	202,149,245	208,632,875	(6,483,630)	(3%)
Net assets, restricted	\$ 148,778,723	\$ 135,654,956	\$ 13,123,767	10%

Statement of Revenues Expenses and Changes in Fund Net Assets

	2010	2009	Variance	% increase (decrease)
Operating revenue	\$ 13,015,518	\$ 13,083,579	\$ (68,061)	(1%)
Operating expense	12,029,461	12,634,545	(605,084)	(5%)
Operating income	986,057	449,034	537,023	120%
Non operating revenue	12,137,710	8,795,601	3,342,109	38%
Change in net assets	\$ 13,123,767	\$ 9,244,635	\$ 3,879,132	42%

Statement of Cash Flows

	2010	2009	Variance	% increase (decrease)
Net Cash provided by (used in) operating activities	\$ 1,716,748	\$ (1,764,433)	\$ 3,481,181	(197%)
Net cash (used) provided by non- capital and related financing activities	3,450,571	3,531,482	(80,911)	(2%)
Net increase (decrease) in cash and cash equivalents	\$ 5,167,319	\$ 1,767,049	\$ 3,400,270	192%

Financial Highlights

- The Authority closed nine new loans totaling \$16,649,584.
- The Authority received a federal capitalization grant in the amount of \$20,187,600.
- Net assets increased \$13,123,767 mainly due to the utilization of \$14,379,271 in federal funds transferred to loan recipients.

Alabama Drinking Water Finance Authority
Statement of Net Assets
September 30, 2010

	Business-type Activities
Assets	
Current assets:	
Cash and cash equivalents - restricted	\$ 45,644,583
Due from ADEM	500,000
Accrued interest receivable on investments - restricted	182,295
Accrued interest receivable on loans receivable	995,528
Current portion of loans receivable	11,785,000
Grants and other receivables	312,458
Accrued arbitrage rebate	163,147
Total current assets	59,583,011
Noncurrent assets:	
Investments - restricted	54,763,753
Loans receivable less unamortized premium of \$5,494,729	227,260,271
Principal forgiveness	5,766,997
Unamortized bond issue cost	3,553,936
Capital assets, net	-
Total noncurrent assets	291,344,957
Total assets	350,927,968
Liabilities	
Current liabilities:	
Accounts payable	21,564
Current portion of revolving loan bonds	6,815,000
Accrued interest payable	1,043,425
Due to Alabama Department of Environmental Management (ADEM)	1,157,787
Total current liabilities	9,037,776
Long-term liabilities:	
Payables to municipalities	26,376,453
Revolving loan bonds payable, less unamortized discount of \$714,984	166,735,016
Total long-term liabilities	193,111,469
Total liabilities	202,149,245
Net Assets	
Restricted for loans and debt service	148,778,723
Total net assets	\$ 148,778,723

See accompanying notes.

Alabama Drinking Water Finance Authority
Statement of Activities
For the Year Ended September 30, 2010

Functions/Programs	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Business-type Activities
Business-type Activities:				
Drinking water loans	\$ 16,012,464	\$ 1,646,653	\$ 14,379,271	\$ 13,460
General Revenues				
Investment earnings				13,110,307
Change in net assets				13,123,767
Net Assets - beginning				135,654,956
Net Assets - ending				\$ 148,778,723

See accompanying notes.

Alabama Drinking Water Finance Authority
Statement of Net Assets
Proprietary Fund
September 30, 2010

	Business-type Activities - Enterprise Funds		
	Loan Fund	Loan Fee Fund	Total
Assets			
Current assets:			
Cash and cash equivalents - restricted	\$ 41,728,646	\$ 3,915,937	\$ 45,644,583
Due from ADEM	500,000	-	500,000
Accrued interest receivable on investments - restricted	182,295	-	182,295
Accrued interest receivable on loans receivable	995,528	-	995,528
Current portion of loans receivable	11,785,000	-	11,785,000
Grants and other receivables	312,458	-	312,458
Accrued arbitrage rebate	163,147	-	163,147
Total current assets	55,667,074	3,915,937	59,583,011
Noncurrent assets:			
Investments - restricted	54,763,753	-	54,763,753
Loans receivable less unamortized premium of \$5,494,729	227,260,271	-	227,260,271
Principal forgiveness	5,766,997	-	5,766,997
Unamortized bond issue cost	3,553,936	-	3,553,936
Capital assets, net	-	-	-
Total noncurrent assets	291,344,957	-	291,344,957
Total assets	347,012,031	3,915,937	350,927,968
Liabilities			
Current liabilities:			
Accounts Payable	-	21,564	21,564
Current portion of revolving loan bonds	6,815,000	-	6,815,000
Accrued interest payable	1,043,425	-	1,043,425
Due to ADEM	-	1,157,787	1,157,787
Total current liabilities	7,858,425	1,179,351	9,037,776
Long-term liabilities:			
Payables to municipalities	26,376,453	-	26,376,453
Revolving loan bonds payable, less unamortized discount of \$714,984	166,735,016	-	166,735,016
Total long-term liabilities	193,111,469	-	193,111,469
Total liabilities	200,969,894	1,179,351	202,149,245
Net Assets			
Restricted for loans and debt service	146,042,137	2,736,586	148,778,723
Total net assets	\$ 146,042,137	\$ 2,736,586	\$148,778,723

See accompanying notes.

Alabama Drinking Water Finance Authority
Statement of Revenues, Expenses, and Changes in Fund Net Assets
Proprietary Fund
For the Year Ended September 30, 2010

	Business-type Activities - Enterprise Funds		
	Loan Fund	Loan Fee Fund	Total
Operating Revenues			
Investment earnings	\$ 2,307,635	\$ 2,619	\$ 2,310,254
Interest from loan receivable	9,058,611	-	9,058,611
Administrative fees	-	1,646,653	1,646,653
Total operating revenues	11,366,246	1,649,272	13,015,518
Operating Expenses			
Administration expense	1,859,937	-	1,859,937
Bond interest expense	8,488,053	-	8,488,053
Bond discount amortization expense	81,063	-	81,063
Bond issuance amortization expense	242,280	-	242,280
Depreciation	-	14,602	14,602
Employee benefits	-	225,714	225,714
Office expense	-	184,129	184,129
Other expenses	-	256,471	256,471
Salaries	-	677,212	677,212
Total operating expenses	10,671,333	1,358,128	12,029,461
Operating income	694,913	291,144	986,057
Nonoperating Revenues (Expenses)			
Grant revenue	14,379,271	-	14,379,271
Principal forgiveness expense	(3,983,003)	-	(3,983,003)
Net increase in the fair value of investments	1,741,442	-	1,741,442
Total nonoperating revenues	12,137,710	-	12,137,710
Change in net assets	12,832,623	291,144	13,123,767
Net Assets - beginning of year	133,209,514	2,445,442	135,654,956
Net Assets - end of year	\$ 146,042,137	\$ 2,736,586	\$ 148,778,723

See accompanying notes.

Alabama Drinking Water Finance Authority
Statement of Cash Flows
Proprietary Fund
For the Year Ended September 30, 2010

	Business-type Activities - Enterprise Funds		
	Loan Fund	Loan Fee Fund	Total
Cash Flows from Operating Activities:			
Interest and dividends received on investments	\$ 2,375,096	\$ 2,619	\$ 2,377,715
Interest paid on revolving loan bonds	(8,632,443)	-	(8,632,443)
Receipts of payments from municipalities	12,100,000	-	12,100,000
Payments to employees and vendors	-	(164,175)	(164,175)
Interest received on loans receivable	7,997,348	-	7,997,348
Administration fees	(1,859,937)	1,646,653	(213,284)
Payments to municipalities	(9,926,472)	-	(9,926,472)
Payments to ADEM	(500,000)	(1,321,941)	(1,821,941)
Net cash provided by (used in) operating activities	1,553,592	163,156	1,716,748
Cash Flows from Non-capital and Related Financing Activities:			
Grant revenue received	14,458,932	-	14,458,932
Principal forgiveness expense	(6,699,585)	-	(6,699,585)
Net redemptions of investment securities	2,101,224	-	2,101,224
Principal paid on revolving loan bonds	(6,410,000)	-	(6,410,000)
Net cash provided by non-capital and related financing activities	3,450,571	-	3,450,571
Net increase in cash and cash equivalents	5,004,163	163,156	5,167,319
Cash and Cash Equivalents - restricted, beginning of year	36,724,483	3,752,781	40,477,264
Cash and Cash Equivalents - restricted, end of year	\$ 41,728,646	\$3,915,937	\$ 45,644,583

-continued-

See accompanying notes.

Alabama Drinking Water Finance Authority
Statement of Cash Flows (Continued)
Proprietary Fund
For the Year Ended September 30, 2010

	Business-type Activities - Enterprise Funds		
	Loan Fund	Loan Fee Fund	Total
Reconciliation of Operating Income to Net Cash Provided by (Used in)			
Operating Activities:			
Operating income	\$ 694,913	\$ 291,144	\$ 986,057
Bond discount amortization	81,063	-	81,063
Bond issuance amortization	242,280	-	242,280
Depreciation	-	14,602	14,602
(Increase) decrease in operating assets:			
Due from ADEM	(500,000)	-	(500,000)
Accrued interest receivable on investments - restricted	67,461	-	67,461
Accrued interest receivable on loans receivable	(17,531)	-	(17,531)
Loans receivable	1,106,268	-	1,106,268
Increase (decrease) in operating liabilities:			
Accounts payable	-	21,564	21,564
Accrued interest payable	(35,630)	-	(35,630)
Payables to municipalities	23,528	-	23,528
Accrued arbitrage rebate	(108,760)	-	(108,760)
Due to ADEM	-	(164,154)	(164,154)
 Net cash provided by (used in) operating activities	 \$ 1,553,592	 \$ 163,156	 \$ 1,716,748

See accompanying notes.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 1 - DESCRIPTION OF ORGANIZATION

The Alabama Drinking Water Finance Authority (the "Authority"), a component unit of the State of Alabama, was created by the State of Alabama's Legislature in 1997 to issue revolving loan bonds and lend the bond proceeds to eligible municipalities at below market interest rates to pay for certain costs of planning, designing, acquiring or constructing certain sanitary drinking water and related facilities. The Federal Water Quality Act of 1987, as amended by the Federal Safe Drinking Water Act Amendment of 1996 (SDWA), provides for the implementation of a state revolving loan program to accept the federal capitalization grants and the required 20% state matching funds which are provided by the federal and state governments. The Alabama Department of Environmental Management (ADEM) is the recipient agency of the federal grant and has been designated by the State of Alabama to administer the revolving loan program.

The Authority does not have any full time employees. Instead, ADEM charges the Authority for time spent on revolving loan program activities by employees of ADEM, and the Authority reimburses ADEM for such costs. The charges include the salaries and benefits of the employees, as well as indirect costs allocated to the Authority based on direct salary costs. Employees charging time to the Authority are covered by the benefits of ADEM.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. In accordance with Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and the Governmental Entities that Use Proprietary Fund Accounting*, the Authority has elected to apply all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) pronouncements and Accounting Principles Board Opinions, issued on or before and subsequent to November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect reported amounts of assets and liabilities at the date of the balance sheet and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Restricted Assets

Under each bond indenture, certain funds and bank accounts are required to be established and controlled by a trustee. The accounts of the trustee funds are maintained on the cash receipts and disbursements basis and are adjusted for financial statement purposes to reflect accrued receivables and payables. Additional restricted assets are held by the State of Alabama on behalf of the Authority until the disbursement of the assets to municipalities occurs.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Subsequent Events

The Authority has evaluated subsequent events through February 8, 2011, the date the financial statements were available to be issued.

Cash and Cash Equivalents

Highly liquid investments with a maturity of 90 days or less when acquired are classified as cash equivalents. Included in cash equivalents are money market funds and repurchase agreements held by the State Treasurer. Money market funds are held by a counterparty or by its trust department but not in the Authority's name. The repurchase agreements held by the State Treasurer are held in the Authority's name.

Investments

Investments are reported at fair value. All investment income, including changes in the fair value of investments, is recognized in the statement of revenues, expenses, and changes in net assets. Repurchase agreements are stated at cost, which approximates market value. The Authority has not adopted a formal written investment policy. However, as disclosed in Note 3, investments and underlying collateral are limited to U.S. Government Securities and AAA rated investments.

Bond Discount and Issue Costs

Bond discounts on long-term debt are amortized on the interest method over the life of the debt to which it relates. Bond issue costs are capitalized and amortized using the straight-line method over the life of the respective issues.

Loans Receivable, Payables to Municipalities, and Loan Premium

The Authority issues loans to eligible municipalities or their agencies (municipalities) through the purchase of the municipalities' revenue or general obligation bonds or warrants with the loan disbursements being made as the municipalities' construction expenditures are incurred. The loans to municipalities are in excess of the expenditures made by the Authority. The excess of these loans receivables over the payments to municipalities is classified as a loan premium. This loan premium, which allows the Authority to recover certain costs associated with the loan, is amortized into income on the interest method over the life of the loan. The stated interest rate for these loans range from 3.05% to 3.95% and the effective interest rates range from 3.05% to 4.42%. The loans are typically repaid over a twenty-year period. The stated interest rates for these loans include a 0.75% fee charged to municipalities for administrative costs.

Payables to municipalities represent amounts committed by the Authority to fund qualifying projects conducted by the municipalities.

No provision for uncollectible accounts has been made, as all loans are current, and Management believes that all loans will be repaid according to the loan terms.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Capital Assets

Capital assets are recorded at cost and are being depreciated over their estimated useful lives. The estimated useful life of the Authority's capital assets is three years. Depreciation is calculated using the straight-line method. The Authority maintains a capitalization threshold of five hundred dollars. The cost of normal maintenance and repairs that do not add to the asset value or materially extend useful lives are not capitalized.

Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the Authority are interest earnings on loans and investments. Due to the nature of the Authority's business, obtaining and making loans, interest which is typically nonoperating is deemed to be operating revenue. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Administrative Fees

The sole source of administrative fees is a 0.75% fee charged to municipalities on the principal amount of the loan made to the municipalities by the Authority, net of bank and trustee fees.

Grant Revenue

Grants received are recognized as nonoperating revenues in the accounting period in which they are earned and become measurable. The federal capitalization grant is awarded in the form of a letter of credit. Funds are drawn from the federal capitalization grant only after the originating expenditure to the municipality has been approved. Since expenditure is the primary factor for determining eligibility, revenue is recognized when the funds are expended.

The State appropriation is awarded to the Authority by the State legislature each year. In accordance with federal law, the appropriation must be at least 20% of the federal capitalization grant. The State's appropriation is not expended upon receipt; therefore, the State's appropriation is deferred upon receipt and recognized as revenue as a constant percentage of each federal grant draw. Such percentage is dependent on the actual appropriation (see Note 6).

Interfund Transfers

The Authority has the ability to transfer and receive funds from the Clean Water State Revolving Fund. No interfund transfers were made during 2010.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Budget Information

Under the Alabama Constitution, money may only be drawn from the Treasury by a legal appropriation. However, the Authority operates under a continuous appropriation because the funding of the matching funds approved by the voters contained its own appropriation authority. Therefore, the Authority's operations are not included in the State's annual budget.

Concentration of Credit Risk

All of the loans to municipalities represent receivables from municipalities located in the State of Alabama.

NOTE 3 – CASH AND INVESTMENTS

Deposits

As of September 30, 2010, cash consisted of non-interest bearing deposits held by the State Treasurer and financial institutions in the name of the Authority. The Authority's deposits were covered by the Federal Deposit Insurance Corporation (FDIC) or by collateral held with the State Treasurer's office in the name of the State Treasurer under the Security for Alabama Funds Enhancement (SAFE) Act. Under the SAFE Act, financial institutions holding public deposits in excess of the amounts insured by the FDIC must pledge collateral to a collateral pool in the name of the State Treasurer. The State Treasurer is responsible for monitoring compliance with the collateralization and reporting requirements of the SAFE Act. If any member financial institution fails, the entire collateral pool becomes available to satisfy claims of governmental entities. If the value of the pool's collateral were inadequate to cover the loss, additional amounts would be assessed on a pro rata basis to the members of the pool. Funds deposited in accordance with the requirements of the SAFE Act are considered fully secured.

Investments

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The fair value of fixed-maturity investments fluctuates in response to changes in market interest rates. Increases in prevailing interest rates generally translate into decreases in fair value of those instruments. The fair value of interest sensitive instruments may also be affected by the creditworthiness of the issuer, prepayment options, relative values of alternative investments, and other general market conditions. Certain fixed maturity investments have call provisions that could result in maturity, and as such, fixed maturity investments are classified in the following table as if they were held to maturity. The Authority has no policy on interest rate risk.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 3 – CASH AND INVESTMENTS (Continued)

As of September 30, 2010, the Authority had the following investment holdings and maturities:

		Investment Maturities		
	Market	Less than 3 years	3-6 years	Greater than 6 years
Investments:				
U.S. Treasury Strips	\$ 9,461,618	\$ 1,811,925	\$ 1,713,058	\$ 5,936,635
Repurchase Agreements	5,942,675	-	-	5,942,675
Guaranteed Investment Contracts	29,634,694	-	-	29,634,694
U.S. Treasury Bonds/Notes	9,724,766	-	-	9,724,766
Total investments	54,763,753	\$ 1,811,925	\$ 1,713,058	\$ 51,238,770
Cash Equivalents:				
Repurchase agreements held by State Treasurer	24,332,135	\$ 24,332,135	\$ -	\$ -
Money Market Funds	21,312,448	N/A	N/A	N/A
Total cash equivalents	45,644,583	\$ 24,332,135	\$ -	\$ -
Total holdings	\$ 100,408,336			

Custodial Credit Risk – Custodial credit risk is the risk that in the event of the failure of the counterparty to a transaction, the Authority will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Authority has U.S. Government securities (bonds, notes, strips, and repurchase agreements) totaling \$25,129,059 held in trust by either the Bank of New York or U.S. Bank in a fiduciary capacity. These securities are bond reserve funds and are held under a trust agreement between the Authority and the trustee bank for the benefit of the bondholder and are not deemed to have custodial credit risk. The securities are approved by bond insurers and are held in the name of the Trustee for the bond issue for the benefit of bondholder. The Authority has custodial credit risk relative to repurchase agreements through the State Treasury whose policy requires that the underlying securities held in the counterparty's safekeeping department be in the name of the Authority. The Authority has no policy for custodial credit risk.

Investments Exposed to Custodial Credit Risk

Repurchase agreements through State Treasurer \$ 24,332,135

Concentration of Credit Risk – Concentration of credit risk is the result of investing 5% or more of total investments in any one issuer. The Authority has no policy for concentration of credit risk. As of September 30, 2010, the Authority entered into Guaranteed Investment Contracts with the following issuers that comprised 5% or more of total investment holdings:

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 3 – CASH AND INVESTMENTS (Continued)

Issuer	Investment Type	Fair Value	Percentage of Total Holdings
AIG	Guaranteed Investment Contracts	\$ 17,033,667	16.88%
Citigroup	Guaranteed Investment Contracts	6,311,028	6.25%

Credit Risk – Credit Risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. Nationally recognized statistical rating organizations provide ratings of debt securities' quality based on a variety of factors, such as financial condition of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations. The bond indenture agreements authorize the Authority to invest in "eligible investments." "Eligible investments" are defined as (a) any debt securities that are direct, general obligations of the United States of America; (b) any debt securities where the payment of the principal and of interest on which is unconditionally guaranteed by the United States of America; and (c) repurchase agreements collateralized by securities of the type described in the preceding clauses (a) and (b) above with any commercial bank, of such broker/dealer subject to the Securities Investors' Protection Corporation jurisdiction or any commercial bank if such broker/dealer or bank has an uninsured, unsecured, and unguaranteed obligation rated "Prime-1" or "A-3" or better by Moody's Investors Service, Inc. and "A-1" or "A-" or better by Standard & Poor's Corporation. All of the investments and cash equivalents held by the Authority for the year ended September 30, 2010 are collateralized by U.S. Government securities rated AAA by Moody's Investor Services.

The ratings of total holdings are as follows at September 30, 2010:

Moody's Ratings	Fair Value	Fair Value as a Percent of Total Holdings Value
Exempt from disclosure	\$ 19,186,384	19.01%
AAA	21,812,448	21.62%
Not rated	59,909,504	59.37%
	<u>\$ 100,908,336</u>	<u>100.00%</u>

Investment holdings that are exempt from disclosure consist of U.S. Treasury strips, bonds, and notes. Investment holdings that are not rated consist of repurchase agreements. Repurchase agreements are not rated by Moody's Investors Service. The underlying collateral for the repurchase agreements was rated AAA by Moody's Investors Service at September 30, 2010.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 4 – LOANS RECEIVABLE

Loans receivable at September 30, 2010, as discussed below, are as follows:

Completed projects	\$ 183,035,000
Projects in progress	61,505,000
	<u>244,540,000</u>
Less:	
Current portion loans receivable	11,785,000
Unamortized premium	5,494,729
	<u>17,279,729</u>
Loans receivable, net	<u>\$ 227,260,271</u>

Loans mature at various intervals. The schedule of principal payments on loans maturing in subsequent years as follows:

2011	\$ 11,785,000
2012	12,670,000
2013	13,260,000
2014	13,925,000
2015 and thereafter	192,900,000
	<u>\$ 244,540,000</u>

As of September 30, 2010, the Authority's ten largest outstanding loans, in the aggregate, exceeded \$117 million. The outstanding balances of these loans represent approximately 48% of the total loans receivable, as follows:

Loan Recipient	Balance
Shelby County South Water Treatment Plant (Supplemental)	\$ 25,065,000
Shelby County South Water Treatment Plant	20,915,000
Shelby County South Water Treatment Plant	15,200,000
Albertville Water Treatment & Distribution Improvements	12,840,000
Madison Water System Improvements	8,705,000
Harvest-Monrovia Water Improvements	7,505,000
West Morgan-East Lawrence Drinking Water Infrastructure Improvements	7,380,000
Madison Co. WTP and Storage Tanks	6,870,000
Tuscaloosa Water System Improvements	6,515,000
Harvest-Monrovia Water Improvements (Supplemental)	6,440,000
	<u>\$ 117,435,000</u>

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 5 – CAPITAL ASSETS, NET

Capital assets consist of the following depreciable assets at September 30, 2010:

	Balance 10/1/2009	Additions	Deletions	Balance 9/30/2010
Data processing equipment	\$ 283,175	\$ -	\$ -	\$ 283,175
Scientific and technical equipment	185,473	-	-	185,473
	468,648	-	-	468,648
Less: Accumulated depreciation	454,046	14,602	-	468,648
Total capital assets, net	\$ 14,602	\$ (14,602)	\$ -	\$ -

NOTE 6 – APPROPRIATIONS

During the year ended September 30, 2010, the U. S. Environmental Protection Agency (EPA) awarded ADEM capitalization funds under its annual grant agreement in the amount of \$16,823,000. As of September 30, 2010, no funds had been expended under this grant. During the year ended September 30, 2010, the State of Alabama did not appropriate any funds from the State General Fund to the Authority.

The federal capitalizing grants require a state appropriation of at least 20% of the awarded federal capitalization grant. In the absence of such an appropriation, the EPA allows the required match to be satisfied by using a portion of the proceeds from the revolving fund loan bonds. The Authority has chosen to use bond proceeds as the required match for the federal capitalizing grants. As of September 30, 2010, the Authority had yet to receive any state matching funds.

The amount of unused federal capitalization grants was approximately \$31,347,904 at September 30, 2010. The Authority will apply for a federal capitalization grant in 2010. Any grants in 2010 and subsequent years are subject to approval on a yearly basis.

The following summarizes the capitalization grant awarded, amounts drawn on each grant, and balances available for future loans as of September 30, 2010:

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 6 – APPROPRIATIONS (Continued)

Year	Grant Amount	Draws prior to 2010	2010 Draws	Total Draws	Amount Available for Future Draws
2007	\$ 8,229,000	\$ 7,283,762	\$ 945,238	\$ 8,229,000	\$ -
2008	8,146,000	6,997,711	1,148,289	8,146,000	-
2009	8,146,000	-	4,499,240	4,499,240	3,646,760
2009-A	19,500,000	-	8,621,856	8,621,856	10,878,144
2010	16,823,000	-	-	-	16,823,000
	<u>\$ 60,844,000</u>	<u>\$ 14,281,473</u>	15,214,623	<u>\$ 29,496,096</u>	<u>\$ 31,347,904</u>
Less:					
	Administrative and set-aside expenses		(755,691)		
	Total 2010 Draws		<u>\$ 14,458,932</u>		

NOTE 7 – PAYABLES TO MUNICIPALITIES

As of September 30, 2010, the authority had \$26,376,453 in payable to municipalities. These payables represent loans on projects in progress at year end. Loan funds are advanced as work is completed on each project.

NOTE 8 – LONG-TERM DEBT

On September 1, 1998, the Authority issued Series 1998A Revolving Fund Loan Bonds totaling \$36,785,000. The Series 1998A bonds include:

\$28,605,000 serial bonds commencing August 15, 1999 and due August 15, 2017, which bear interest at rates ranging from 4.00% to 4.80%.

\$8,180,000 term bonds due August 15, 2022, which bears interest at 4.85%.

On February 1, 2000, the Authority issued Series 2000A&B Revolving Fund Loan Bonds totaling \$14,130,000. The Series 2000A&B bonds include:

\$5,130,000 Series 2000A serial bond commencing August 15, 2000 and due August 15, 2015, which bear interest at rates ranging from 4.10% to 5.85%.

\$3,475,000 Series 2000A term bonds due August 15, 2021, which bear interest at 6.00%.

\$5,525,000 Series 2000B term bonds due August 15, 2021, which bear interest at 8.35%.

On December 1, 2000, the Authority issued Series 2000C Revolving Fund Loan Bonds totaling \$25,895,000. The Series 2000C bonds include:

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 8 – LONG-TERM DEBT (Continued)

\$12,075,000 serial bonds commencing February 15, 2001 and due February 15, 2014, which bear interest at rates ranging from 4.30% to 5.50%.

\$5,615,000 term bonds due August 15, 2018, which bear interest at 5.75%.

\$8,205,000 term bonds due August 15, 2023, which bear interest at 5.38%.

On January 1, 2002, the Authority issued Series 2002A Revolving Fund Loan Bonds totaling \$37,575,000. The Series 2002A Bonds include:

\$12,955,000 serial bonds commencing February 15, 2002, and due August 15, 2012, which bear interest at rates ranging from 3.00% to 4.75%.

\$3,245,000 term bonds due August 15, 2014, which bear interest at 5.07%.

\$3,620,000 term bonds due August 15, 2016, which bear interest at 5.22%.

\$4,050,000 term bonds due August 15, 2018, which bear interest at 5.32%.

\$7,050,000 term bonds due August 15, 2021, which bear interest at 5.40%.

\$6,655,000 term bonds due August 15, 2024, which bear interest at 5.46%.

On December 1, 2003, the Authority issued Series 2003A Revolving Fund Loan Bonds totaling \$38,915,000. The Series 2003A Bonds include:

\$24,805,000 serial bonds commencing February 15, 2004, and due August 15, 2021, which bear interest at rates ranging from 2.00% to 4.50%.

\$7,465,000 term bonds due August 15, 2024, which bears interest at 4.73%.

\$6,645,000 term bonds due August 15, 2027, which bear interest at 4.82%.

On December 1, 2004, the Authority issued Series 2004A Revolving Fund Loan Bonds totaling \$24,880,000. The Series 2004A Bonds include:

\$17,035,000 serial bonds commencing February 15, 2008, and due August 15, 2028, which bear interest at rates ranging from 4.00% to 4.63%.

\$7,845,000 term bonds due August 15, 2026, which bear interest at 4.50%.

On October 1, 2005, the Authority issued Series 2005A Revolving Fund Loan Bonds totaling \$42,580,000. The Series 2005A Bonds include:

\$27,095,000 serial bonds commencing August 15, 2008, and due August 15, 2024, which bear interest at rates ranging from 4.00% to 5.25%.

\$15,485,000 term bonds due August 15, 2028, which bear interest at 4.00%.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 8 – LONG-TERM DEBT (Continued)

All bond issues contain provisions in which the Authority may, at its option and without premium, redeem amounts equal to amounts on deposit in the Capitalized Interest Account and the Bond Proceeds Account, generally within three years of the second payment date.

All bonds are insured by a municipal bond insurance policy for the total of the principal and interest. The bond insurer (AMBAC Indemnity) will not insure payment on acceleration or the payment of any redemption, prepayment, acceleration premium or any risk other than nonpayment.

Summary of changes in long-term debt for 2010:

	Balance 10/1/09	Additions	Reductions	Balance 9/30/10
Revolving fund loan bonds	\$ 180,675,000	\$ -	\$ 6,410,000	\$ 174,265,000
Less: Unamortized discounts	796,047	-	81,063	714,984
Total	\$ 179,878,953	\$ -	\$ 6,328,937	\$ 173,550,016

Long-term debt at September 30, 2010 is payable as follows:

	Principal	Interest	Total
2011	\$ 6,815,000	\$ 8,347,401	\$ 15,162,401
2012	7,290,000	8,026,514	15,316,514
2013	7,925,000	7,683,354	15,608,354
2014	8,255,000	7,304,144	15,559,144
2015	9,200,000	6,905,359	16,105,359
2016-2020	55,120,000	26,913,369	82,033,369
2021-2025	55,895,000	12,511,035	68,406,035
2026-2028	23,765,000	1,957,269	25,722,269
	174,265,000	<u>\$ 79,648,445</u>	<u>\$ 253,913,445</u>
Less:			
Unamortized discount	714,984		
Current portion of long-term debt	6,815,000		
	<u>\$ 166,735,016</u>		

NOTE 9 – ARBITRAGE REBATE CALCULATIONS

In accordance with Internal Revenue Code, Section 148, and related regulations as the issuer of tax-exempt debt, the Authority has calculated a rebate of \$163,147 due from the Internal Revenue Service at September 30, 2010.

Alabama Drinking Water Finance Authority

Notes To Financial Statements

NOTE 10 – RELATED PARTIES

ADEM acts as an agent for the Authority and is authorized to administer the revolving loan fund program in accordance with applicable federal and state laws. The director of ADEM is the vice president of the Authority. ADEM receives a portion of the federal capitalization grants as reimbursement for administrative costs.

NOTE 11 – PRINCIPAL FORGIVENESS

During the year ended September 30, 2009, the EPA awarded ADEM capitalization funds under the American Recovery and Reinvestment Act of 2009 (ARRA) in the amount of \$19,500,000. This grant provided for the recipient (ADEM) to use at least 50% of the funds provided by the grant to provide additional subsidization in the form of principal forgiveness, negative interest rate loans, or grants. Therefore, principal forgiveness in the aggregate amount of \$9,750,000 was allocated amongst qualifying projects for the municipalities. This amount was initially shown as a receivable on the statement of net assets and was included in the total amount payable to municipalities. Principal forgiveness is stated separately from the associated loans receivable as it is not required to be repaid by the municipalities. As the work is completed on these projects and the loan funds are advanced to the municipalities, a percentage of the total principal forgiveness amount is expensed in relation to the total amount paid to the respective municipalities. Principal forgiveness expense recognized during the year ended September 30, 2010 totaled \$3,983,003, leaving a remaining balance of \$5,766,997 capitalized as principal forgiveness on the statement of net assets as of September 30, 2010.

SUPPLEMENTARY INFORMATION

Alabama Drinking Water Finance Authority
Schedule of Expenditures of Federal Awards
September 30, 2010

Federal Grantor/Pass Through Grantor/Program Title	CFDA Number	Grantor's Number	Federal Expenditures
Environment Protection Agency			
Passed through the Alabama Department of Environmental Management			
Capitalization grants for state revolving funds	66.468	FS984472-07	\$ 731,438
Capitalization grants for state revolving funds	66.468	FS984472-08	839,482
Capitalization grants for state revolving funds	66.468	FS984472-09	4,620,709
ARRA - Capitalization grants for state revolving funds	67.468	2F954280-09	8,187,642
Total Environmental Protection Agency			14,379,271
Total federal financial assistance			\$ 14,379,271

Alabama Drinking Water Finance Authority
Notes To Schedule of Expenditures of Federal Awards
For the Year Ended September 30, 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies and presentation of the Single Audit Report of the Alabama Drinking Water Finance Authority (the "Authority") have been designed to conform to generally accepted accounting principles as applicable to governmental units, including the reporting and compliance requirements of the Audits of States, Local Governments, and Non-Profit Organizations and Office of Management and Budget Circular A-133, Compliance Supplement (A-133).

Reporting Entity – The Authority consists of the Loan Fund and the Loan Fee Fund, both of which are Enterprise Funds. The Authority included a schedule of federal financial assistance in the Single Audit section.

Basis of Accounting – Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied.

The modified accrual basis of accounting is followed in the Schedule of Expenditures of Federal Awards. Under the modified accrual basis of accounting, revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the current period. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recorded when the related liability is incurred. In applying the susceptible-to-accrual concept to intergovernmental revenues, the legal and contractual requirements of the numerous individual programs are used as guidance. There are, however, essentially two types of such revenues. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the Authority; therefore, revenues are recognized based upon the expenditures recorded. In the other, monies are virtually recognized based upon the expenditures recorded. In the other, monies are virtually unrestricted as to purpose of expenditure and substantially irrevocable; i.e., revocable only for failure to comply with prescribed compliance requirements, such as with equal employment opportunity. These resources are reflected as revenues at the time of receipt or earlier if they meet the availability criteria.

NOTE 2 – CONTINGENCIES

Grant monies received and disbursed by the Authority are for specific purposes and are subject to review by the grantor agencies. Such audits may result in requests for reimbursement due to disallowed expenditures. Based upon prior experience, the Authority does not believe that such disallowance, if any, would have a material effect on the financial position of the Authority. As of February 8, 2010, there were no material questioned or disallowed costs as a result of grant audits in process or completed.

COMPLIANCE SECTION

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Alabama Drinking Water Finance Authority
Montgomery, Alabama

We have audited the accompanying financial statements of the business-type activities, the major fund, and the remaining fund information of the Alabama Drinking Water Finance Authority (the "Authority"), as of and for the year ended September 30, 2010, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated February 8, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in **Government Auditing Standards**, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under **Government Auditing Standards**.

We noted certain matters involving internal control over financial reporting which we have reported to management in a separate letter dated February 8, 2011.

This report is intended solely for the information and use of management, the board members and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Carr, Riggs & Ingram, L.L.C.

CARR, RIGGS & INGRAM, L.L.C.

Certified Public Accountants

February 8, 2011

**INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE
WITH OMB CIRCULAR A-133**

Board of Directors
Alabama Drinking Water Finance Authority
Montgomery, Alabama

Compliance

We have audited the compliance of Alabama Drinking Water Finance Authority (the "Authority") with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each of its major federal programs for the year ended September 30, 2010. The Authority's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Authority's management. Our responsibility is to express an opinion on the Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in **Government Auditing Standards**, issued by the Comptroller General of the United States, and OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations". Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Authority's compliance with those requirements.

In our opinion, the Authority complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended September 30, 2010.

Internal Control Over Compliance

The management of the Authority is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the Authority's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, the board members, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Carr, Riggs & Ingram, L.L.C.

CARR, RIGGS & INGRAM, L.L.C.

Certified Public Accountants

February 8, 2011

**Alabama Drinking Water Finance Authority
Schedule of Findings and Questioned Costs
For The Year Ended September 30, 2010**

SECTION I - Summary of Auditors' Results

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified ☐ yes ☒ no
- Reportable condition(s) identified that are not considered to be material weaknesses? ☐ yes ☒ none reported

Noncompliance material to financial statements noted? ☐ yes ☒ no

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? ☐ yes ☒ no
- Reportable condition(s) identified that are not considered to be material weakness(es)? ☐ yes ☒ none reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? ☐ yes ☒ no

Identification of major programs:

CFDA Numbers

Name of Federal Program or Cluster

66.468

Capitalization Grants for Drinking Water State Revolving Funds

Dollar threshold used to distinguish between type A and type B programs? \$ 431,378

Auditee qualified as low-risk auditee? ☒ yes ☐ no

SECTION II – Financial Statements Findings

No matters were reported.

SECTION III – Federal Award Findings and Questioned Costs

No matters were reported.